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1945

Economic Conditions
Governmental Finance
United States Securities

New York, April, 1945

General Business Conditions

THE military news at the time this Letter goes to press admits no other interpretation than that Germany is rapidly approaching, if she has not already reached, a state of disorganization which will end in collapse; and the longer she resists the greater is the disorganization and the more certain the collapse becomes. One-third of her 1937 territory, with a normal population of some 25 million out of 70 million people, is in the hands of the Allied or Russian armies. The loss of raw materials, foodstuffs and industrial resources proportionately is even greater. With Upper Silesia, the Saar and the Rhineland occupied, the great Ruhr Basin surrounded, and important districts East of the Rhine being overrun at a sensational rate, the Reich has few basic resources left to supply her war effort. Major transportation and communication lines have been cut and are constantly bombed, and breakdowns in transportation disrupt both military and economic activity.

It is true that many manufacturing centers of Central Germany and Czechoslovakia may not be overrun for some time, if the German armies can be rallied and redeployed. Some commentators have argued that the German war effort can be maintained a long time by operation of these plants, which include many dispersed in remote areas or put underground during the war. But this view seems to overlook the loss of coal, steel and other raw materials from the Ruhr, Saar and Upper Silesia, and of the food production of the eastern territories. Even the most effectively dispersed and protected war industries can not function long after major sources of fuel and materials are cut off, nor can their work be integrated and their products distributed without adequate transportation. Germany must draw more and more on accumulated stores of materials and stocks of finished munitions. Her armies are fighting with this knowledge and with the evidence of economic disintegration before them.

Disruption of German Economy

With the coal fields of the Ruhr and German Silesia cut off, Germany now controls only 10 per cent of the prewar bituminous production of her own territory and Czechoslovakia. She still has three-fourths of her lignite, which however contains on the average only about one-fourth the heat units of bituminous coal. Altogether, it is probable that Germany now controls no more than the equivalent of 70 to 75 million tons of good coal annually, compared with 275 million for the "Greater Reich" in 1939; and the most important Czech field is within range of Russian guns. Bituminous coal was the basis for the German war effort. Without plentiful supplies, the synthetic oil plants will be crippled; the operation of new blast furnaces built in Central Germany to utilize local low-grade iron ore deposits will be handicapped; and the output of electricity (36 per cent was derived from bituminous coal) will be affected.

In semi-manufactures the looming shortage of steel is the most important. Capacity remaining to Germany is probably less than one-third of the 1939 figure, or less than 10 million tons. Considerable aluminum capacity is still available, but Germany no longer has access to the bauxite deposits in France, Western Hungary and Yugoslavia. More than half of her lead and zinc were lost in Upper Silesia. All these figures refer only to lost territory; no allowance for the effects of bombing on territory still held is included.

Finally, the area still under German control produces considerably less than its normal food requirements. Yet there are probably 15 to 25 million more people to be fed, owing to evacuations from the occupied areas and the presence of foreign workers and prisoners of war. Drastic food measures had been taken before the Allied break across the Rhine. The Reich Agricultural Commissioner ordered last month the killing of all livestock except milch cows, hens, and breeding stock in general, to reduce consumption of potatoes and grain. Another order required a drastic curtailment

of food distribution from one part of the Reich to another; each section is supposed to draw mainly on local resources.

Available reports indicate that the Reich's finances are as disorganized as her economy, with the currency system breaking down and widespread resort to barter. At the outbreak of the war the various types of German marks in use were quoted at figures ranging up to the official rate of 40c in American money, but a recently published quotation in Switzerland placed the mark at 2500 to the dollar or 1/25th of one cent.

Effects on Domestic Situation

The military news brings into view the question of the adjustments in the domestic situation to be expected at the end of the war in Europe. The general nature of these adjustments is apparent. The aggregate need for munitions will be diminished and more resources can be devoted to non-military output. The most definite indication of the extent of the cutback in war production is that given by Mr. Byrnes in his second quarterly report as Director of War Mobilization and Reconversion. He said deliveries of finished munitions for the Army Service Forces would be reduced 15 to 20 per cent within three months after V-E day and 40 per cent within twelve months. Figures for the Army Air Forces and th Navy, which will have to be included to arrive at an overall total, are not yet ready; but their cuts doubtless will be less than those of the ground forces.

Announcement of these figures coincides with an increase of concern, evident in the Washington agencies, for maintenance of the civilian economy. There is much testimony that essential industries, essential services and essential workers need greater consideration in the allocation of goods and materials if the industrial organization is to be kept functioning effectively. Last Summer plans and preparations were made for increasing production of essential civilian goods, but they were swallowed up by the demands for greater munitions output when it developed that the German war would last longer than expected; and few of these preparations have borne any fruit. On the contrary, restrictions on the use of materials and labor for civilian goods have steadily tightened, and the pinch is being felt more keenly than before.

Now the cycle seems ready to take another turn. Moves are under way by the Washington agencies which aim at determination of rock-bottom essential non-military requirements, not to be encroached upon. Thus Mr. Krug, chairman of the War Production Board, apparently feels that allocations of steel to transportation facilities have been cut too close and talks of trimming military allocations accordingly. The appointment by Mr. Byrnes of the Crowley Committee to allocate exports, the protest of Mr. Byrnes' Advisory Committee against being ignored in recent policy decisions, and the action of Congress in limiting Lend-Lease strictly to war requirements, are other indications in the same direction.

The Business Outlook

The business prospect after V-E day hinges upon employment. The effect of cutbacks in war production is to release labor from war plants, and the evidence from scattered industrial centers where cutbacks have occurred is that trade promptly reflects the drop in employment, although these instances are obscured in record-breaking retail trade for the country as a whole. This induces a spirit of hesitation. On the other hand, it is hardly disputable, as a general statement, that civilian requirements can readily absorb the labor and materials likely to be released from war work in the first few months after V-E day, as rapidly as plants can be converted, labor shifted and necessary civilian inventories accumulated. The extent of civilian needs and of civilian buying power is a buoyant influence on sentiment.

The strongest influence on the situation after V-E day will be the handling of reconversion problems, such as contract settlement, clearing factories of war machinery and inventory, retooling, retraining labor, disposition of price and materials controls, and all the others. Mr. Krug has made a statement to the effect that W.P.B. has never ceased planning of reconversion procedure, and a set of principles now being followed has been made public. Points included are that privately-owned facilities will be released from war work before government-owned plants; that cutbacks will be pro-rated as far as possible among prime contractors; that plants will get one week's notice of contract termination; and that when contracts are completed or terminated every possibility of putting new war work into the plant or transferring its workers to new war jobs will be canvassed before permitting civilian production. This is along the lines of the "spot authorization" plan, which is now largely moribund because plants authorized to resume civilian production have not been able to get materials to do so.

These policies are suited to present conditions, when aggregate war production is still expanding, and individual cutbacks are limited. A new set of principles will be called for, however, when cutbacks become the rule rather than the exception and when the facilitation of reconversion becomes a major objective. Difficult questions, such as when and in what manner controls may be removed, how to assure fair and equitable treatment for com-

petitive interests, and many others, will then become urgent. During the coming weeks discussion of these questions is certain to rise. There will doubtless be occasion to return to them in this Letter.

Corporate Earnings in 1944

In our March issue we gave a preliminary summary of corporate earnings for 1944 limited to the manufacturing industries. Large numbers of additional reports have been issued during the past month, and we are now presenting a much broader and more comprehensive summary of results not only in manufacturing but also in mining, trade, transportation, public utilities, service and finance. In 1944 there was a further increase in volume of sales or operating revenues, but the rise was less than during the two preceding years, reflecting the flattening of the upward curve as capacity was reached. The continuing advance in labor and material costs resulted in a further lowering of profit margins, but the high federal income taxes tended to stabilize net income by offsetting to a considerable extent any decreases or increases in operating earnings.

Aggregate net income of a group of 2,665 leading corporations last year was approximately $5,241 million after taxes, compared with $5,266 million in 1943, a decrease of 0.5 per cent. The 1944 earnings of companies having war contracts are subject to renegotiation in most cases, but are shown after deduction of reserves, if any, for such renegotiation as well as for postwar costs and contingencies. In a number of cases the 1943 earnings as originally reported have been revised downward where renegotiation resulted in larger payments to the Government than had been provided for by reserves.

Aggregate capital and surplus of the group at the beginning of 1944 was $63,589 million, upon which the year's net income represented an average return of 8.2 per cent, compared with a net worth of $61,414 million in 1943 and a return of 8.6 per cent. The changes by major divisions were as follows, while our more detailed summary by industrial groups is given on the next page.

Summary of Net Income After Taxes of Leading Corporations in 1943 and 1944

(In Millions of Dollars)

No. of Cos.	Division	Net Income 1943	Net Income 1944	% Chg. 1943-44	% Return 1943	% Return 1944
1,327	Manufacturing	$2,730	$2,889	+ 5.9	9.6	9.8
109	Mining, quarry	89	95	+ 7.8	7.2	7.6
143	Trade	235	245	+ 3.9	10.1	10.2
236	Transportation	954	747	—21.7	7.7	5.8
215	Public utilities	633	618	— 2.4	6.6	6.5
92	Service & constr.	89	89	— 0.2	12.5	11.7
543	Finance	537	557	+ 3.9	8.0	7.7
2,665	Total	$5,266	$5,241	— 0.5	8.6	8.2

In the manufacturing industries reports are now available for 1,327 companies, and in most lines show trends similar to those indicated by our preliminary summary. Total sales increased by about 10 per cent to a new peak, and combined net income of the group was up 6 per cent, due principally to increases in the petroleum and in some of the food, beverage, chemical, metal products and transportation equipment industries. About 53 per cent of all manufacturing companies reporting showed decreases in net income last year, against 47 per cent showing increases.

A supplementary table given below of 941 manufacturing companies reporting sales figures shows aggregate sales of $59,799 million last year, upon which the net income after taxes (including income from investments and other sources as well as from sales) was $1,994 million, or an average of 3.3 per cent. This compared with 3.6 per cent in 1943 and 7.5 per cent in 1940, and was the lowest since the depression year 1934.

Percentage of Net Income after Taxes to Sales of Leading Corporations in 1943 and 1944

(In Thousands of Dollars)

No. of Cos.	Manufacturing	Sales 1944	Net Inc.* 1944	% Net Inc. to Sales 1944	% Net Inc. to Sales 1943
16	Baking	$ 744,719	$ 23,198	3.1	3.6
12	Dairy products	1,518,411	32,125	2.1	2.2
15	Meat packing	4,796,977	45,373	0.9	1.1
54	Other food products	2,077,381	89,985	4.3	4.3
39	Beverages	1,429,492	57,980	4.1	4.4
13	Tobacco products	1,543,852	65,468	4.2	4.5
31	Cotton goods	612,412	18,935	3.1	3.2
42	Other textile products	1,061,546	29,498	2.8	4.3
23	Leather and shoes	611,009	19,016	3.1	3.5
19	Rubber products	2,558,701	67,969	2.7	3.0
19	Wood products	363,805	13,565	3.7	3.3
52	Pulp, paper products	871,976	39,048	4.5	5.0
41	Chemical products	1,291,183	70,258	5.4	6.2
19	Drugs, soap, etc.	1,006,271	65,128	6.5	7.4
12	Paint and varnish	435,309	14,877	3.4	3.1
28	Petroleum products	3,855,692	268,777	7.0	6.8
42	Stone, clay and glass	1,043,187	51,032	4.9	5.1
41	Iron and steel	6,283,484	164,560	2.6	2.8
8	Agricul. implements	1,530,839	56,870	3.7	4.5
27	Bldg.,heat.,plum.equip.	743,529	29,887	4.0	3.9
35	Electrical equipment	4,500,468	129,048	2.9	3.0
83	Machinery	1,814,585	58,105	3.2	3.9
14	Nonferrous metals	693,739	59,947	8.6	9.0
105	Other metal products	2,958,851	112,088	3.8	4.4
17	Autos and trucks	7,211,271	221,585	3.1	3.2
42	Auto equipment	1,620,356	44,853	2.8	3.1
14	Railway equipment	1,073,060	33,661	3.1	3.1
27	Aircraft and parts	4,323,637	52,684	1.2	1.3
51	Other manufacturing	1,223,121	58,048	4.7	4.7
941	Total manufacturing	59,798,863	1,993,568	3.3	3.6
	Trade				
10	Chains—food	1,664,001	16,217	1.0	1.0
42	Chains—other	2,597,106	89,498	3.4	3.6
32	Department stores	1,553,383	43,251	2.8	3.0
6	Mail order	1,720,418	56,834	3.3	3.5
26	Misc. and wholesale	1,130,478	26,806	2.4	2.4
116	Total trade	$8,665,386	$232,606	2.7	2.8

* Net income, after taxes, includes income from investments and other sources as well as from sales.

Reports of 116 companies in the various branches of retail and wholesale trade gave sales figures last year aggregating $8,665 million, an increase of about 9 per cent over 1943. Because of higher costs of goods, operating expenses and taxes, however, there was an increase of but 4 per cent in net income. The latter represented an average of 2.7 cents per dollar of sales, compared with 2.8 cents in 1943 and 3.9 cents in 1940, and was lower even than the margins in 1933-34.

NET INCOME OF LEADING CORPORATIONS FOR THE YEARS 1943 AND 1944

Net Income is Shown after Depreciation, Interest, Taxes, and Other Charges and Reserves, but before Dividends.—Net Worth Includes Book Value of Outstanding Preferred and Common Stock and Surplus Account at Beginning of Each Year.

(In Thousands of Dollars)

No.	Industrial Groups	Net Income After Taxes 1943	Net Income After Taxes 1944	Per Cent Change	Net Worth January 1 1943	Net Worth January 1 1944	Per Cent Return 1943	Per Cent Return 1944
20	Baking	$26,008	$24,889	— 4.3	$266,085	$271,724	9.8	9.2
14	Dairy products	32,209	33,674	+ 4.5	313,210	306,011	10.3	11.0
15	Meat packing	46,537	45,373	— 2.5	628,802	598,949	7.4	7.6
23	Sugar	21,071	34,780	+65.1	341,545	345,241	6.2	10.1
51	Other food products	94,289	95,998	+ 1.8	829,180	864,700	11.4	11.1
19	Soft drinks	40,172	39,318	— 2.1	166,646	180,275	24.1	21.8
26	Brewing	8,847	9,472	+ 7.1	62,027	66,356	14.3	14.3
8	Distilling	38,688	45,261	+17.0	254,114	272,340	15.2	16.6
20	Tobacco products	79,375	74,270	— 6.4	784,828	799,431	10.1	9.3
41	Cotton goods	28,293	24,107	—14.8	327,683	339,581	8.6	7.1
12	Silk and rayon	17,260	16,885	— 2.2	241,903	244,449	7.1	6.9
7	Woolen goods	9,659	8,747	— 9.4	100,230	105,652	9.6	8.3
16	Knitted goods	6,296	6,358	+ 1.0	63,815	65,865	9.9	9.7
36	Other textile products	26,902	26,523	— 1.4	276,492	298,752	9.7	8.9
23	Clothing and apparel	11,563	10,863	— 6.1	109,855	113,990	10.5	9.5
9	Leather tanning	4,411	3,911	—11.3	43,769	45,019	10.1	8.7
18	Shoes, etc.	17,596	15,688	—10.8	193,131	197,089	9.1	8.0
22	Rubber products	64,854	68,996	+ 6.4	541,671	586,642	12.0	11.8
20	Lumber	8,156	9,070	+11.2	92,103	98,498	8.9	9.2
12	Furniture, wood products	6,529	7,799	+19.5	93,966	95,326	6.9	8.2
74	Pulp and paper products	51,157	51,932	+ 1.5	690,778	711,188	7.4	7.3
23	Printing and publishing	10,151	11,378	+12.1	106,276	111,433	9.6	10.2
54	Chemical products	187,718	200,379	+ 6.7	1,792,481	1,882,536	10.5	10.6
25	Drugs, soap, etc.	72,045	69,327	— 3.8	407,133	436,698	17.7	15.9
18	Paint and varnish	17,555	20,729	+18.1	258,515	261,930	6.8	7.9
39	Petroleum products	498,922	624,922	+25.3	6,196,788	6,443,010	8.1	9.7
22	Cement, gypsum, etc.	11,076	6,609	—40.3	230,371	241,762	4.8	2.7
40	Other stone, clay and glass	55,149	57,088	+ 3.5	576,377	600,504	9.6	9.5
54	Iron and steel	198,547	186,510	— 6.1	3,552,768	3,605,807	5.6	5.2
12	Agricultural implements	61,134	60,297	— 1.4	689,528	697,957	8.9	8.6
42	Bldg., heat., plumb. equipment	34,005	35,689	+ 5.0	364,265	378,302	9.3	9.4
58	Electrical equipment	128,549	143,697	+11.8	1,045,245	1,100,321	12.3	13.1
48	Hardware and tools	45,808	40,993	—10.5	350,188	362,507	13.1	11.3
31	Household equipment	13,998	15,029	+ 7.4	128,800	133,109	10.9	11.3
121	Machinery	95,293	86,377	— 9.4	695,552	734,339	13.7	11.8
17	Office equipment	29,052	30,394	+ 4.6	250,611	257,937	11.6	11.8
24	Nonferrous metals	171,116	144,855	—15.3	1,834,968	1,871,158	9.3	7.7
59	Other metal products	54,634	64,405	+17.9	566,592	594,196	9.6	10.8
20	Autos and trucks	202,185	223,887	+10.7	1,633,179	1,741,589	12.4	12.9
52	Auto equipment	54,463	57,863	+ 6.2	343,029	373,437	15.9	15.5
20	Railway equipment	36,390	38,528	+ 5.9	400,168	413,634	9.1	9.3
29	Aircraft and parts	65,161	69,130	+ 6.1	237,207	292,495	27.5	23.6
4	Shipbuilding	5,309	5,421	+ 2.1	22,878	26,085	23.2	20.8
29	Misc. manufacturing	41,379	42,392	+ 2.4	369,322	389,068	11.2	10.9
1,327	Total manufacturing	2,729,511	2,889,813	+ 5.9	28,474,059	29,556,892	9.6	9.8
25	Coal mining	23,697*	29,384*	+24.0	546,388	559,006	4.3	5.3
31	Metal mining	25,183*	21,354*	—15.2	355,868	351,088	7.1	6.1
43	Oil and gas	27,583*	30,911*	+12.1	233,547	247,882	11.8	12.5
10	Other mining, quarrying	12,093*	13,779*	+13.9	96,930	97,618	12.5	14.1
109	Total mining, quarrying	88,556*	95,428*	+ 7.8	1,232,733	1,255,594	7.2	7.6
13	Chain stores — food	17,690	19,112	+ 8.0	211,408	216,162	8.4	8.8
44	Chain stores — other	89,278	89,942	+ 0.7	773,576	800,104	11.5	11.2
36	Department stores	43,928	45,925	+ 4.5	485,075	497,821	9.1	9.2
6	Mail order	53,634	56,834	+ 6.0	554,821	575,554	9.7	9.9
44	Misc. and wholesale	30,804	32,784	+ 6.4	309,967	318,658	9.9	10.3
143	Total trade	235,334	244,597	+ 3.9	2,334,847	2,408,299	10.1	10.2
127	Class 1 railroads (a)	873,932	667,614	—23.6	11,256,510	11,728,078	7.8	5.7
43	Traction and bus	36,193	29,517	—18.4	495,721	514,164	7.3	5.7
8	Shipping	8,812	8,051	— 8.6	124,537	128,310	7.1	6.3
11	Air transport	10,670	15,611	+46.3	55,629	69,125	19.2	22.6
47	Misc. transportation	24,359	26,492	+ 8.8	382,689	386,476	6.4	6.9
236	Total transportation	953,966	747,285	—21.7	12,315,086	12,821,153	7.7	5.8
165	Electrical power, gas, etc. (a)	432,404	424,238	— 1.9	6,653,154	6,607,548	6.5	6.4
50	Telephone and telegraph (a)	201,012	193,962	— 3.5	2,946,113	2,947,602	6.8	6.6
215	Total public utilities	633,416	618,200	— 2.4	9,599,267	9,555,150	6.6	6.5
17	Amusements	58,185	61,481	+ 5.7	450,137	486,773	12.9	12.6
34	Restaurant and hotel	12,652	11,143	—11.9	93,057	94,567	13.6	11.8
28	Other business services	12,791	13,551	+ 5.9	114,156	120,848	11.2	11.2
13	Construction	5,245	2,531	—51.7	54,829	56,108	9.6	4.5
92	Total service and construction	88,873	88,706	— 0.2	712,179	758,296	12.5	11.7
163	Commercial banks	289,381	327,103	+13.0	3,281,327	3,475,841	8.8	9.4
79	Fire and casualty insurance	107,116	85,388	—20.3	1,076,180	1,233,705	10.0	6.9
139	Investment companies	100,057	111,632	+11.6	1,740,561	1,876,949	5.7	5.9
54	Sales finance companies	38,461	30,398	—21.0	500,696	483,574	7.7	6.3
108	Real estate companies	1,494	2,933	+96.3	147,338	143,543	1.0	2.0
543	Total finance	536,509	557,454	+ 3.9	6,746,102	7,213,612	8.0	7.7
2,665	Grand total	$5,266,165	$5,241,483	— 0.5	$61,414,278	$63,568,996	8.6	8.2

* Before depletion charges in some cases. (a) In this group, due to the large proportion of capital investment in the form of funded debt, the rate of return on total property investment would be lower than that shown on net worth only.

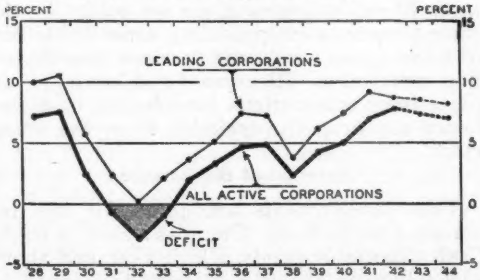
Railroad and Utility Earnings

The railroads last year surpassed all previously established records in the volume of freight and passenger traffic. While total operating revenues of the 127 Class 1 systems were about 4 per cent higher, total wage and salary payments were 9 per cent higher, and net railway operating income was 19 per cent lower. Net income after interest charges and all taxes was $668 million compared with $874 million in 1943, a decline of 24 per cent.

Reports of a group of 165 leading public utility systems supplying electric, gas and other services show a combined increase last year of about 5 per cent in gross revenues. There was a slightly larger increase in total operating expenses and taxes, however, and net income was down by 2 per cent. The numbers reporting increases and decreases in net were about equally divided, and in most cases the changes were relatively small.

Earnings of all Corporations

The accompanying chart covering the seventeen-year period 1928-44 shows the average rate of return on net worth of leading corporations, as given in our annual tabulations of published shareholders' reports, and also the rates for all active corporations in the United States, as compiled by the Treasury Department, Bureau of Internal Revenue, from tax returns and given in the annual Statistics of Income (Part II, Corporations).



Annual Rate of Return on Net Worth of All Active Corporations and of Leading Corporations

Average rates for leading corporations, from National City Bank annual tabulations of published shareholder's reports, were:

1928____10.0	1932____0.2	1936____7.4	1940____7.4
1929____10.6	1933____2.1	1937____7.2	1941____9.2
1930____5.7	1934____3.6	1938____3.8	1942____8.7
1931____2.4	1935____5.1	1939____6.2	1943____8.6
			1944____8.2

Data for all corporations appear in the table following.

A summary of the official Treasury statistics is given in the table below. This shows two series: (1) Net income after taxes, excluding intercorporate dividends received from other domestic corporations (which for the corporate system as a whole do not represent real income but merely transfers), together with gross income, and the average percentage margin of profit; and (2) Net income after taxes, including intercorporate dividends received, together with total net worth (the portion of which held by other corporations is not reported separately), and the average rate of return. Total dividends paid out, excluding intercorporate dividends, are also shown. Figures for 1942 are preliminary, and those for 1943 and 1944 are estimated.

All Active Corporations in the U. S.

(In Millions of Dollars)

Year	Gross Income-a	Net Income After Tax-a	Net to Gross Income %	Net Worth Jan.1	Net Income After Tax-b	Rate of Return %	Net Dividends Paid-a
1928	$151,888	$7,566	5.0	$132,408	$ 9,483	7.2	$5,157
1929	158,565	8,084	5.1	142,887	10,677	7.5	5,927
1930	134,017	1,366	1.0	160,369	3,937	2.5	5,631
1931	106,088	—3,145	—3.0	161,282	—1,176	—0.7	4,182
1932	80,378	—5,375	—6.7	148,363	—4,115	—2.9	2,626
1933	83,208	—2,379	—2.9	133,569	—1,353	—1.0	2,101
1934	99,278	162	0.2	127,578	2,379	1.9	2,672
1935	111,636	1,674	1.5	141,585	4,688	3.3	2,927
1936	130,046	3,903	3.0	138,981	6,580	4.7	4,702
1937	139,761	3,872	2.8	133,468	6,554	4.9	4,832
1938	118,663	1,480	1.2	141,633	3,271	2.3	3,222
1939	130,972	4,040	3.1	137,437	5,946	4.3	3,841
1940	146,216	4,779	3.3	136,864	6,800	5.0	4,068
1941	188,197	7,272	3.9	138,887	9,507	6.9	4,466
1942-p	216,336	9,750	4.5	142,591	11,094	7.8	4,263
1943-e	250,000*	9,580	3.8	146,500*	11,060	7.5	4,110
1944-e	275,000*	8,490	3.1	150,000*	10,050	7.0	4,325

Source: Compiled from Treasury Department annual "Statistics of Income." (a) Excludes intercorporate dividends. (b) Includes intercorporate dividends. (e) Estimate by Treasury Department. (p) Preliminary. — Deficit. * Unofficial rough estimate.

It will be seen that the great expansion in volume of business after 1938, stimulated by the outbreak of war in Europe and later carried to unprecedented heights after our entrance into the war, was accompanied by a rising level of net income through 1941 or 1942. The expansion in volume permitted a much fuller and hence more profitable use of the country's plant and equipment facilities, as well as manpower. It called into use the so-called "marginal" producers, which can operate at a profit only in times when the demand for their goods and services is unusually high. Much of the rise in the earnings of all business corporations, taking the combined figures of those having deficits with those having net income, has resulted merely from the elimination or reduction of deficits.

The fact that the rate of return shown on the chart for leading corporations declined slightly in 1942, whereas that for all corporations continued to rise, may have been caused chiefly by two factors. First, the Treasury figures show "net income" as defined for tax purposes, and before allowance for contingency and postwar reserves, which are not allowable deductions in computing taxes, thus raising the net income correspondingly over that shown on published shareholders' reports. Second, the official statistics, covering some 469,000 active corporations, include many thousands of closely-held businesses which publish

no financial statements but whose earnings—speaking generally, and recognizing many exceptions—have risen much more sharply than have those of the larger organizations.

Since 1942 the net earnings of the larger corporations in most fields have been stabilized to considerable extent by the maintenance of near-capacity operations combined with the wartime price controls, renegotiations of government contracts, and the high income tax rates. For business as a whole, the tremendous increase in gross revenues since 1942 has not been reflected in higher earnings, but in larger disbursements for labor and other operating costs. Under the present tax rates (95 per cent on excess profits and an 80 per cent over-all ceiling) rising costs not only narrow profit margins, but also reduce taxable income and the taxes payable thereon. The recently published United States Steel Corporation report revealed that the $30 million estimated cost of the retroactive wage adjustment ordered by the War Labor Board last November reduced the corporation's taxes $25.7 million, so that (except for such relatively small individual income taxes as may be recovered from the recipients), 85½ per cent of the cost of the award was borne by the Treasury, which means the public at large. The effect of rising costs in cutting down corporate earnings was recognized by the Treasury last year when its previous estimate of the 1944 net income after taxes of all corporations, which had indicated an increase of $850 millions over 1943, was lowered to indicate a decrease of $1,090 million.

U. S. Wartime Balance of Payments

On a number of occasions we have discussed in this Letter the great changes which the war has brought about in the international balance of payments of the United States. On trade and service account, Lend-Lease excluded, the balance has run heavily against us. We have lost gold, and foreigners have accumulated bank deposits and other short-term funds in such amounts that our total obligations to foreigners now exceed our assets abroad. In short, we have ceased to be a creditor nation, at least temporarily, and have become an international debtor.

To measure these changes, there is now available the first official summary of our wartime balance of payments, published by the Bureau of Foreign and Domestic Commerce in "Foreign Commerce Weekly" of March 10. The figures, which in part are only estimates, cover the period 1940-44. They bring out forcefully the shift in our international transactions. In tabulating them we have condensed the figures, added data for the year 1939, and grouped the totals into three pre-Pearl Harbor and three post-Pearl Harbor years.

U. S. Balance of International Payments, 1939-1944

(In Millions of Dollars)

	1939-41 Inc.	1942-44 Inc.
Goods and Services		
Excess of merchandise exports	+3,407	—
Excess of merchandise imports	—	—1,747
Net services bought (incl. milit. exp.)	—1,076	—3,151
Net goods and service transactions	+2,331	—4,898
Financial Transactions, Capital Movements		
Debt service and dividends (net)	+1,101	+ 945
Long-term cap'l outflow (—), inflow (+)		
American (net)	— 156	+ 143
Foreign (net)	— 525	+ 57
Short-term cap'l outflow (—), inflow (+)		
American (net)	+ 325	+ 53
Foreign (net)	+1,681	+ 253
Net financial and capital transactions	+2,426	+1,451
Balance of all above transactions	+4,757	—3,447
Balancing Items		
Loss (+) or gain (—) of gold	—7,685	+2,155
Increase (+) or decrease (—) in foreign official dollar funds	+ 886	+1,615
Residual item, inflow (+), outflow (—)	+2,042	— 323
	—4,757	+3,447

Source: Foreign Commerce Weekly, March 10, 1945, except the figures for 1939, for which the data from "The United States In The World Economy" were used; the 1939 figures are not precisely comparable with those of 1940-44.

As will be seen, the most significant change took place in goods and service transactions. These include, in addition to our sales and purchases of merchandise and such services as shipping, also the amounts sent abroad by our tourists, immigrants, and charitable organizations. Whereas in the three years before Pearl Harbor we sold foreigners $2.3 billion more goods and services than we bought from them, in 1942-44 we bought from abroad almost $5 billion more than we sold. At the same time we were providing some $35 billion of Lend-Lease goods and services (less $4 billion received in "Reverse Lend-Lease"), but these huge transactions involved no cash and hence are properly excluded from the statement.

Reversal of the Balance

Two developments accounted for this reversal of the balance. One was a shift in trade. Cash exports of goods, which averaged about $3.9 billion in the 1939-41 period, dropped to about $3 billion in the three years 1942-44. At the same time our imports after Pearl Harbor averaged over $800 million a year more than in the 1939-41 period, reflecting largely the increased need of raw materials for our war industries.

The other main cause of our heavy debit balance was a sharp rise in the outlay of dollars for services performed for us by foreigners. From $1/4 billion in 1940 the annual average of these net payments rose to over $1 billion, mainly because of the great expansion in our military expenditures overseas. To quote the Department of Commerce, "next to merchandise imports, military expenditures have become, for the time being, the most important factor supplying dollars to foreign countries."

The Department did not report these expenditures separately, but it did say that because of incomplete reports the total is understated in the overall estimate. Among other things, no adjustment was made for a still undetermined additional amount of dollars due to such countries as France or Italy for advances of francs and lire to our armed forces.

Due predominantly to these changes, our calculated balance of payments (before allowing for gold shipments) ran $3.5 billion against us in the three post-Pearl Harbor years as compared with a balance of $4.8 billion in our favor in the 1939-41 period. This unfavorable balance was met in part by shipment of $2.2 billion of gold and the remainder added to foreign funds held here.

Changes in Our Creditor-Debtor Position

On long-term account, our net creditor position apparently has been little affected by our wartime transactions with the outside world. According to the Department of Commerce, our long-term investments abroad in September 1944 exceeded the long-term investments of foreigners in the United States by about $4½ billion. This was approximately the same amount as at the end of 1939; a precise comparison is difficult because, as will be seen from the table below, the 1944 figures cover a wider ground and include also U. S. Government investments made abroad during the war.

U. S. International Investment Position, Exclusive of War Debts

(In Billions of Dollars)

	Dec., 1939	Sept., 1944
U. S. Investment Abroad		
Long-term Investments		
Direct	7.0	7.3
Foreign dollar bonds	3.8*	1.7†
Miscellaneous private	n.r.	1.0
U. S. Government	n.r.	.6
Total long-term	10.8	10.6
Short-term investments	.6	.5
Total U. S. assets abroad	11.4	11.1
Foreign Investments in U. S.		
Long-term investments		
Direct	2.0	2.2
U. S. bonds and stocks	} 4.3	3.4
Miscellaneous		.6
Total long-term	6.3	6.2
Short-term investments	3.3	6.1
Total U. S. liabilities	9.6	12.3
Net Investment Position		
On long-term account	+4.5	+4.4
On short-term account	—2.7	—5.6
Total	+1.8	—1.2

* Valued at par. † Market value. n.r. = not reported.

Source: The 1939 figures: "The U. S. in The World Economy", Economic Series No. 23; the 1944 figures: "International Investment Position of United States", Foreign Commerce Weekly, January 27, 1945.

Our short-term debts, however, have been almost doubled by our wartime transactions, while our overseas short-term holdings have remained practically unchanged. Foreign short-term balances in this country were built up from about $3.3 billion at the end of 1939, to over $6 billion in September 1944, according to Department of Commerce figures. This increase has converted our overall creditor position of 1939 (combining long- and short-term accounts) to a debtor position in 1944.

In longer perspective, the decline in the creditor position of this country which set in after 1930 has thus gone to the point where the credit balance built up during and after World War I and in the decade in the '20s has given way to a debit balance, in overall terms. The decline was due at first to cessation of foreign lending and to shrinkage in value, and redemptions and repatriation, of our outstanding loans and investments. Later the inflow of foreign capital here, seeking refuge and stability, was the important factor. During the war the shift in our position has continued, as shown in the table, as a consequence of trade and military transactions.

To many people the information that this country is no longer "the world's greatest creditor nation" but on balance of foreign assets and liabilities not even a creditor nation at all, doubtless comes as a surprise, since so much comment as to our international obligations is based on our assumed creditor position. It is true that the wartime adverse balance in our current payments in all likelihood will prove transitory, since military expenditures will cease; foreign countries will want American goods after the war and are almost certain to use some of their $6 billion of short-term funds to get what they want; and we on our part, with our great productive capacity and great power to generate capital, will almost as certainly provide loans and investments for foreign reconstruction and development. Nevertheless, the fact that the United States will enter the postwar period owing more to foreigners than foreigners owe to us is of profound significance. Foreign assets here will be of immense aid in the transition and reconstruction period.

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